No. 17-494

IN THE

Supreme Court of the United States

SOUTH DAKOTA,

Petitioner,

v.

WAYFAIR, INC., OVERSTOCK.COM, INC., AND NEWEGG, INC.,

Respondents.

On Writ of Certiorari to the Supreme Court of South Dakota

BRIEF FOR COLONY BRANDS, INC. AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENTS

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INTEREST OF *AMICUS CURIAE*[1]

Colony Brands, Inc. (originally known as The Swiss Colony, Inc.) is a Wisconsin corporation that directly or indirectly owns a majority interest in many different corporate subsidiaries and their divisions and brands, including Montgomery Ward, The Swiss Colony, Seventh Avenue, Midnight Velvet, Ginny's, Monroe and Main, Country Door, Ashro, The Tender Filet, and The Wisconsin Cheeseman. All these subsidiaries are catalog mail-order and electronic retail businesses that, in the aggregate, feature extensive offerings to United States consumers in furniture, home decor, apparel, housewares, entertainment products, electronics, and a variety of food products. Combined, they are one of the largest privately-owned direct marketers in the United States and compete with companies located both inside and outside of the United States, including Canada. While today a majority of Colony Brands' subsidiaries' orders from consumers are received by telephone or online attributable mostly to catalog advertising, Colony Brands' subsidiary companies and brands still receive tens of millions of dollars each year from mailed-in orders. In reliance on the "physical presence" substantial nexus standard reaffirmed in

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[1] Pursuant to Supreme Court Rule 37.6, counsel for *amicus* represents that no counsel for a party authored this brief in whole or in part, and no party or counsel for a party made a monetary contribution intended to fund the preparation or submission of this brief. Frank W. Cawood contributed funds for the preparation or submission of this brief. On January 31, 2018 and February 5, 2018, respectively, Petitioner and Respondents gave blanket consent to amicus briefs. These blanket consents were docketed more than 10 days before the due date of this brief.

Quill Corp. v. North Dakota,[2] each of these retailers making consumer sales collects and remits sales taxes in only the select handful of states in which the retailer has chosen to have a physical presence. In cases where they do not collect and remit sales taxes, the consumers are required to pay use taxes on those transactions; and, where required by state law, the retailers report annual summaries of transactions to the consumers and/or the applicable departments of revenue.

A decision by this Court abrogating the principles reinforced in *Quill* – namely the requirement that a retailer must have a physical presence in a state for that state to force it to collect and remit sales taxes – will have a significant negative impact on the businesses of Colony Brands and its subsidiaries. For that reason and others, Colony Brands has an institutional interest in this case and supports the position of Respondents that the decision of the South Dakota Supreme Court should be affirmed.

SUMMARY OF ARGUMENT

This case raises the question of whether, and to what extent, the Constitution sets limits on the ability of states to collect sales and use taxes from out-of-state sellers.

Petitioner South Dakota asks this Court to abrogate *Quill*'s reaffirmation of the bright line "physical presence" test to show a business's "substantial nexus" with a taxing authority under the Commerce Clause. Pet'r Br. at 17-21. The United States argues in support of Petitioner that the states have ample

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[2] 504 U.S. 298 (1992).

authority to collect sales taxes from remote sellers because the accessibility of their websites in a state creates a "virtual presence" there. U.S. Br. at 7-10.

Together, Petitioner and the United States effectively request that the Court pave the way for states to impose on any seller of products, no matter how remote their relation to that state may be, a legal obligation to monitor each and every transaction that leads to a "delivery" within the state for the purpose of ensuring compliance with the state's statutory tax collection regime. This monitoring obligation would attach regardless of the location or domicile, domestic or foreign, of the seller and of the purchaser and regardless of the level of actual presence in the taxing state. And, assuming that a state's unilaterally-determined thresholds are met, the remote seller then would be required to collect and remit state sales and use taxes for every transaction that results in a delivery to that state. The seller would be subject to that state's enforcement jurisdiction, regardless of the scope and extent (if any) of its actual contacts or presence in the state. An Illinois resident's purchase of goods from a New York retailer for delivery to South Dakota would trigger this monitoring requirement and South Dakota's enforcement jurisdiction. South Dakota also would have enforcement jurisdiction over a Mexico City, Mexico resident's purchase of goods from a Canadian retailer for delivery to South Dakota, and the Canadian retailer would be obligated to monitor its sales for each such occurrence. Constitutional tests would be satisfied on the basis of the "virtual" reality of new technologies.

To date, this Court's decisions have preserved the viability of the centuries-old business model of remote

direct sales, thereby preventing states from imposing unreasonable burdens that might threaten or harm that model of interstate commerce. This continuing viability is now under review on the basis of technological innovations that were inconceivable only a few years ago.

The Internet is in the process of revolutionizing the conduct of commerce globally. The Internet, however, is not a physical facility or thing. It is a suite or set of intangible protocols that permits electronic communications networks to interconnect and act as a global system. That system links devices in two-way communication on a worldwide basis. It creates a network of networks consisting of private, public, academic, business, and government networks, both local and global in scope, linked by a broad array of electronic, wireless, and optical networking technologies. It interconnects the globe.

The global system does not in any way, however, transfer the location of the devices it connects and therefore creates no additional presence for those devices. What is virtual is, by definition, not real. It does not create a presence. Unlike the switched telephone connections within older dedicated telephone networks that did create a physical link between sellers and purchasers, the Internet does not even create a tangible connection. Whatever reality it may be perceived to create is entirely virtual, and in that respect its capabilities should be considered to be in their infancy.

Whatever those capabilities may be at any given time, a crucial characteristic of the Internet is that it is a global, and not just an interstate, system. If a remote seller in one state were deemed to have a

presence in another state simply by reason of the accessibility of its website in that state, a remote seller in one country might be deemed to have a presence in another country by reason of the accessibility of its website there.

This case is not just an interstate commerce case. Internet commerce is global commerce, and states must conform their policies to the rules for that commerce that have been established by the United States and its trading partners. Therefore, the tax implications of such a result would require scrutiny, not only under the four-factor analysis of *Complete Auto Transit v. Brady*,[3] but also under the more elaborate inquiry of *Japan Line, Ltd. v. County of Los Angeles*.[4] It would fail that scrutiny. Far from being an "outlier," the physical presence test continues to reflect the international norm for the taxation of global e-commerce.

As such, Petitioner urges this Court to establish a new precedent that would contradict established U.S. and international tax policy and obligations and threaten to undermine the centuries of custom and practice that contributed to the growth of the direct-marketing (including by catalog) industry. It is for the above reasons that the Court's determination in *Quill* – that these matters are best left to Congress – remains as valid today as it was when *Quill* was first decided.

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[3] 430 U.S. 274 (1977).

[4] 441 U.S. 434 (1979).

ARGUMENT

I. STATES ARE OBLIGATED TO CONFORM TO FEDERAL LAW AND POLICY IN THE REGULATION AND TAXATION OF INTERNET SALES

A. The Internet Is A Global System, And The Regulation And Taxation Of Internet Sales Implicates The Foreign Commerce Of The United States

The Internet is a global network connecting hundreds of millions of devices and several billion users in over 190 countries. There are over one billion websites in the world. John Stevens, *Internet Stats & Facts for 2017*, Hosting Facts (Aug. 17, 2017), https://hostingfacts.com/internet-facts-stats-2016/. An assertion of regulatory and/or tax collection jurisdiction by a state that relies on the availability of a website in that state necessarily involves the assertion by that state of its authority over the foreign commerce of the United States. It is not a question of purely interstate commerce. While the states retain a role in interstate commerce subject to the requirements of the Constitution and federal law, the foreign commerce of the United States is "preeminently a matter of national concern." *Japan Line*, 441 U.S. at 449. The states have "no standing" in the realm of foreign relations. *U.S. v. Locke*, 529 U.S. 89, 108 (2000).

B. Where The Foreign Commerce Of The United States Is Implicated, State Action Must Conform To Federal Policy And Practice

The Petitioner argues that a state's assertion of tax collection jurisdiction over the Respondents should be governed not by *Quill*, but by the Court's broader four-

factor analysis set forth in *Complete Auto Transit* (in particular its "substantial nexus" test) and that *Quill's* physical presence test is an "outlier." Pet'r Br. at 22-27. Conversely, the United States argues that not even *Complete Auto Transit* is applicable; rather, the United States suggests that *Pike v. Bruce Church, Inc.*[5] should govern the Court's Commerce Clause analysis of state regulations concerning tax collection.[6] U.S. Br. at 8.

Those arguments are incorrect. Where state action implicates the foreign commerce of the United States, the Court must proceed under the even broader jurisprudence of *Japan Line*. As it applies to the foreign commerce of the United States, the physical presence test would be an "outlier" only if it had not been adopted by the United States (and other countries) as a matter of federal tax law and policy. As demonstrated below, the physical presence test is precisely the test the United States and other nations continue to use in the taxation of e-commerce. As articulated by this Court in *Japan Line*, the United States must be

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[5] 397 U.S. 137 (1970).

[6] Where state regulation has an effect on foreign commerce, "additional scrutiny is necessary to determine whether the regulations 'may impair uniformity in an area where federal uniformity is essential,' or may implicate 'matters of concern to the whole nation ... such as the potential for international retaliation.'" *Pac. Nw. Venison Producers v. Smitch*, 20 F.3d 1008, 1014 (9th Cir. 1994) (internal citations omitted); *see also Japan Line*, 441 U.S. at 446 ("When a State seeks to tax instrumentalities of foreign commerce, two additional considerations, beyond those articulated in [the doctrine governing the Interstate Commerce Clause], come into play."). The application of the balancing analysis set forth in *Pike* does not negate the obligation to consider whether the challenged regulations impair uniformity in an area where federal uniformity is essential.

able to speak with "one voice" in the regulation of the foreign commerce of the United States.[7] It would be fundamentally inappropriate for the several states to assert power over foreign commerce that the United States government itself does not exercise.

In sum, this case is not just an interstate commerce case. Internet commerce is global commerce, and states must conform their policies to the rules for that commerce that have been established by the United States and its trading partners.

C. The United States And The International Community Do Not Recognize The Availability Of A Website As Creating A "Fixed Place of Business" (A "Presence") Within The Jurisdiction Of A Sovereign State

With respect to the taxation of foreign taxpayers in the United States not eligible for the benefits of a tax treaty with the United States, United States tax law generally analyzes whether the foreign taxpayer is engaged in a "trade or business" within the United States (which is a lower threshold than a fixed place of business (*i.e.*, presence)). I.R.C. §§ 872(b), 882(a). Commentators have noted that "[a]t a minimum, for an activity to constitute a trade or business the company's business activities within the United States

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[7] In his amicus brief supporting neither party, Professor John S. Baker argues that the tax collected by South Dakota must be evaluated under the Import-Export Clause and the threefold test articulated by this Court in *Michelin Tire Co. v. Wages*, 423 U.S. 276 (1976). J. Baker Br. at 8-11. That test includes consideration of whether the tax impedes the federal government's ability to "speak with one voice" in conducting the nation's foreign relations. That is the same test articulated in *Japan Line*, which the South Dakota tax collection regime fails.

must be regular, continuous, and profit oriented." David Hardesty, *Electronic Commerce: Taxation & Planning* ¶ 12.02 (Thomson Reuters 2018) (citing *Comm'r v. Groetzinger*, 480 U.S. 23 (1987)). Therefore, commentators have noted that "[i]t is unlikely that a foreign online company will be engaged in the conduct of a [United States trade or business] if it has no physical presence in the United States, and no U.S. agents." *Id.*; *see generally* Office of Tax Policy, U.S. Dep't of Treas., *Selected Tax Policy Implications of Global Electronic Commerce* (Nov. 1996).

In general, the accessibility of a foreign website in the United States, by itself, does not cause a foreign taxpayer to be engaged in a United States trade or business.[8] Commentators state, while discussing the taxation of web servers, that "[t]here seems to be no support for the finding [of] a 'U.S. trade or business' without some actual U.S. presence" and, thus, "[i]t follows that a taxpayer with no activities in the United States could not be engaged in the conduct of a 'U.S. trade or business.'" *See* Hardesty, *supra*, ¶ 12.02[3] (analyzing whether the operation of a web server results in a foreign taxpayer being treated as operating a U.S. trade or business). The same commentator also states, in the context of discussing web servers, that "[i]n most cases, a foreign taxpayer will not be considered to be engaged in the conduct of a U.S. trade or business if neither it nor its agents are regularly performing business activities while present in the United States." *Id.* This determination is partly based

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[8] U.S. tax law taxes the income of a foreign corporation effectively connected with a U.S. trade or business. I.R.C. §§ 872(b), 882(a). To date, the United States has not determined that the accessibility of a website in the United States constitutes a U.S. trade or business.

on *Commissioner of Internal Revenue v. Piedras Negras Broadcasting Co.*,[9] which, in a context different from but analogous to the use of a website, addressed the issue of whether a Mexico company broadcasting radio into the United States would be viewed as doing business simply by accepting payments from customers in the United States.

In *Piedras Negras*, United States-based advertisers compensated a Mexico broadcasting company by sharing gross receipts from United States sales that resulted from ads broadcast by the Mexico company. 127 F.2d at 260. The Mexico company's business was "the operation of a radio broadcasting station located at Piedras Negras, just across the Rio Grande from Eagle Pass, Texas." *Id.* However, the majority of the Mexico company's responses from listeners came from the United States, and 95 percent of its income was from advertisers within the United States. *Id.* With that said, the Mexico company's income-producing contracts were executed in Mexico, and all services required of the Mexico company under the contracts were rendered in Mexico. *Id.* Based on the foregoing, the Fifth Circuit determined that the Mexico company was not treated as doing business in the United States. *Id.* By analogy to *Piedras Negras*, if a foreign company has a website and a web server situated outside the United States and all of the services the foreign company rendered in connection with its website were performed in the foreign country, the foreign company's website should not be treated as doing business in the United States (*i.e.*, a lower threshold than a fixed place of business (*i.e.*, a presence)).

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[9] 127 F.2d 260 (5th Cir. 1942).

With respect to foreign taxpayers that are eligible for the benefits of a tax treaty with the United States, such tax treaties (see, for example, the United States Model Income Tax Convention) generally analyze whether the foreign taxpayer has a "permanent establishment" within the United States. U.S. Model Income Tax Convention, art. 7, § 1; *id.*, art. 5, § 1. Under the United States Model Income Tax Convention, a foreign taxpayer is subject to taxation on business profits in the United States only to the extent those profits are attributable to a permanent establishment in the United States. *Id.*, art. 5, § 1 (stating that "[f]or the purposes of this Convention, the term 'permanent establishment' means a fixed place of business through which the business of an enterprise is wholly or partly carried on"); *id.*, art. 5, § 2 (stating that "[t]he term 'permanent establishment' includes especially: a) a place of management; b) a branch; c) an office; d) a factory; e) a workshop; and f) a mine, an oil or gas well, a quarry, or any other place of extraction of natural resources"). A "permanent establishment" is generally defined by the United States Model Income Tax Convention as "a fixed place of business through which the business of an enterprise is wholly or partly carried on." *Id.*, art. 5, § 1. Therefore, with respect to foreign taxpayers that are eligible for the benefits of a tax treaty with the United States, under the United States Model Income Tax Convention, the question is whether a website, by itself, can create a fixed place of business (*i.e.*, a presence) within the United States. As noted, a commentator has stated that, with respect to whether a website constitutes a United States trade or business (*i.e.*, a lower threshold than a fixed place of business (*i.e.*, a presence)), "[i]t is unlikely that a foreign online company will be engaged in the conduct of a [United States trade or business] if it has no

physical presence in the United States, and no U.S. agents." Hardesty, *supra*, ¶ 12.02 (citing *Groetzinger*, 480 U.S. 23). Therefore, similar to a United States trade or business, the accessibility of a foreign website in the United States does not establish a fixed place of business (*i.e.*, a presence) within the United States.

In this regard, the Organization for Economic Co-operation and Development (OECD)[10] has published guidance regarding whether a website constitutes a permanent establishment and, thus, a fixed place of business (*i.e.*, a presence) in a country. *See* OECD, *Model Tax Convention on Income and on Capital: Condensed Version* art. 5 ¶¶ 42.2, 42.3, 42.4 (2010); *see also* OECD Comm. on Fiscal Affairs, *Clarification on the Application of the Permanent Establishment Definition in E-Commerce: Changes to the Commentary on the Model Tax Convention on Article 5* ¶¶ 42.2, 42.3, 42.4 (2000) (hereinafter, the "OECD Commentaries"), http://www.oecd.org/tax/treaties/1923380.pdf. According to the OECD Commentaries, "a distinction needs to be made between computer equipment, which may be set up at a location so as to constitute a permanent establishment under certain circumstances, and the data and software which is used by, or stored on, that equipment." OECD Commentaries ¶ 42.2. The Commentaries go on to state the following:

> For instance, an Internet web site, which is a combination of software and electronic data, does not in itself constitute tangible property.

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[10] The OECD is an intergovernmental economic organization with 35 member countries, founded in 1961 and headquartered in Paris, France. *See* About OECD, http://www.oecd.org/about/. The mission of the OECD is to promote policies that will improve the economic and social well-being of people around the world. *Id.* The United States is included among the 35 member counties. *Id.*

> It therefore does not have a location that can constitute a "place of business" as there is no "facility such as premises or, in certain instances, machinery or equipment" . . . as far as the software and data constituting that web site is concerned. On the other hand, the server on which the web site is stored and through which it is accessible is a piece of equipment having a physical location and such location may thus constitute a "fixed place of business" of the enterprise that operates that server.

Id. Hardesty notes that "[t]he Commentaries make a careful distinction between a website and a web server because, among other things, the website and web server may each be operated by two separate and independent companies." Hardesty, *supra,* ¶ 11C.03[4][a][i]. The key distinction, consistent with United States tax principles, between a website and a web server is that a (i) website is not comprised of tangible assets and (ii) a web server is comprised of equipment and other tangible assets that can be physically located within a jurisdiction and, thus, constitute a fixed place of business (*i.e.*, a presence). OECD Commentaries ¶¶ 42.2, 42.3, 42.4.

With respect to the authoritative effect of the OECD and the OECD Commentaries, according to a leading commentator in the field of international taxation, "[i]n interpreting a U.S. treaty clause based on a clause in the OECD model treaty, the [Internal Revenue Service] may place great weight on the intent of the model treaty, [and a] court may also look at the OECD model treaty and its commentary." Joel D. Kuntz *et al.*, *U.S. International Taxation* ¶ C4.01[5] (Thomson Reuters 2018). Moreover, many United

States tax treaties "are based on or at least very similar to the OECD Model Tax Convention, so their interpretation may be influenced by the Commentaries." Hardesty, *supra*, ¶ 11C.03[4][a]. In addition, despite the United States not taking an official position with respect to whether a website can create a fixed place of business (*i.e.*, a presence), the United States would, in general, be expected to follow the OECD position.[11] Finally, in a report to Congress, the Advisory Commission on Electronic Commerce proposed "affim[ing] support for the principles of the OECD's framework conditions for taxation of e-commerce, and support[ing] the OECD's continued role as the appropriate forum (1) fostering effective international dialogues concerning these issues and (2) building international consensus." Advisory Commission on Electronic Commerce, *Report to Congress* 42 (2000) (affirming support for the OECD). Based on the foregoing, as one commentator has noted, "[o]ne can only conjecture what the US position might be regarding whether a computer server can create a US trade or business or

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[11] *See* Monica Gianni, *The OECD's Flawed and Dated Approach to Computer Servers Creating Permanent Establishments*, 17 Vand. J. of Ent. & Tech. L. 1, 26 (2014). According to Joseph Guttentag, a former senior U.S. Treasury official, "[t]he [new server and permanent establishment] rules present a reasonable compromise . . . ." Arthur J. Cockfield, *Reforming the Permanent Establishment Principle Through a Quantitative Economic Presence Test*, 38 Can. Bus. L.J. 400, 406 (2003). In addition, when the OECD issued the OECD Article 5 Commentary that treated a web server as a permanent establishment, the United States did not officially object to this position (however, in contrast, the United Kingdom did officially object to the OECD Article 5 Commentary). Gianni, *supra*, at 26; *see also* OECD Commentaries ¶ 45.5.

permanent establishment. Gianni, *supra* note 11, at 27.

In addition to the OECD, other jurisdictions have analyzed whether a website, by itself, can constitute a fixed place of business (*i.e.*, a presence) within a country and, thus, result in a permanent establishment.[12] For example, the Kolkata (India) Tax Tribunal determined that a website, by itself, could not constitute a fixed place of business (*i.e.*, a presence).[13] In *ITO vs. Right Florists Limited*, the Kolkata Tax Tribunal analyzed whether Google (situated in Ireland) and Yahoo (situated in the United States) had permanent establishments in India under the relevant tax treaties. As part of such analysis, the Kolkata Tax Tribunal considered the OECD's commentary that a website, by itself, could not constitute a permanent establishment due to the absence of a fixed place of business (*i.e.*, a presence). Taking the OECD's commentary into account, the Kolkata Tax Tribunal concluded that, because Google and Yahoo did not have a web server in India through which the website

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[12] *See, e.g.*, *ITO v. Right Florists Limited*, I.T.A. No. 1336 (Income Tax Appellate Tribunal, Kolkata, 2011). "The United Kingdom has taken the express position that a server that conducts electronic commerce through a website on the server cannot constitute a permanent establishment." Monica Gianni, *supra* note 11, at 27. "Other countries, including Singapore and Hong Kong, have also officially stated that a server by itself cannot create a permanent establishment." *Id.* The Canadian Revenue Agency has determined that a U.S. company managing applications and data from outside Canada "does not cause the [U.S. company] to have a server at its disposal and, hence, a permanent establishment." *Id.*

[13] *ITO*, I.T.A. No. 1336 at ¶ 28.

was hosted, neither Google nor Yahoo had a permanent establishment in India.

Based on the foregoing, the United States and the international community do not recognize the accessibility of a website as creating a fixed place of business (*i.e.*, a presence) within the jurisdiction of the United States. While the nexus requirements of states may differ from the rules established by the United States and the international community for national tax purposes, the states' assertion of global jurisdiction in contradiction of these rules is a bridge too far.[14] Far from being an outlier, the fixed place of business (*i.e.*, a presence) rule standard is the international norm. Therefore, it follows that the accessibility of a website should not create a fixed place of business (*i.e.*, a presence) within the jurisdiction of a subordinate sovereign. A departure from this standard would set a precedent that would have far reaching implications for international tax policy and the conduct of the foreign economic relations of the United States. Those decisions are necessarily reserved to the Federal Government, specifically to the Executive and to the Congress.

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[14] For an analysis of the complexity of issues surrounding the taxation of global electronic commerce, see Office of Tax Policy, *supra*, at n.10.

II. ASSERTION OF STATE TAX JURISDICTION BY REASON OF THE "ACCESSIBILITY" OF A WEBSITE WOULD UPSET THE FEDERAL SYSTEM OF GOVERNANCE

A. The Virtual Capabilities Of The Internet And Its Related Technologies Are In Their Infancy

In August of 1968, when the Defense Advanced Research Projects Agency ("DARPA")[15] issued a request for quotes for what was to become the Advanced Research Projects Administration Network ("ARPANET"), very few people understood this project's profound implications. In part, ARPANET was designed to connect government, academic, and private research networks to share scarce "high-powered" computer resources. *See* Barry M. Leiner *et al.*, *Brief History of the Internet*, Internet Society (1997), https://www.internetsociety.org/internet/history-internet/brief-history-internet/. ARPANET was designed not to have any direct connections so that if any one connecting network failed, data would continue to flow to its destination over the remaining networks. ARPANET organized information into "packets"[16] and used a common language called Transmission Control Protocol –

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[15] Originally known as the Advanced Research Projects Agency ("ARPA").

[16] A packet is a small unit of data (IP = 128 bits) with a header section and a data section. The header has information about the packet including the sender's address and the recipient's address. A picture sent over the Internet will consist of thousands of packets or more. Those packets will likely not all travel the same path through the various networks to their final destination. See *Layout Showing the Major ISPs*, Internet Mapping Project: Map Gallery, http://www.cheswick.com/ches/map/gallery/isp-ss.gif (a graphic of the major Internet ISP back in 1999) for a small sample of the network of networks comprising part of the Internet.

Internet Protocol ("TCP/IP"). This language and distributed network of networks enabled today's Internet.

Accordingly, the Internet has no separate physical instantiation. The programming language "spoken" on the Internet is the glue that makes this virtual network an incredible resource for government, academic, corporate, and individual users. It was purposely built to avoid the then-vulnerable switched telephone network, which physically connected users (*e.g.*, operators plugging a cord into a console to connect a user to another user locally or long distance). Thus, Internet sales have far less of a physical presence than a company in Delaware mailing a catalog to a person in North Dakota and that person ordering a product over the phone. This is because the Internet was purposefully built *not* to physically connect users.

The Internet is still in its infancy. It was only as recently as 1985 when the 1200-baud modem for Internet connectivity became widely available. This 1200 bits-per-second device enabled email and simple text bulletin boards services. Today, Internet Service Providers are connecting homes at one billion bits per second. Smartphones and high-speed wireless data services make it possible for a Washingtonian in London to use an application[17] (app) on her iPhone and

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Packets have a large number of pathways to their final destination and algorithms determine each packet's path.

[17] By 2017, nearly 6.5 million different mobile applications for smartphones were available for download. *See* Dyfed Loesche, *The Biggest App Stores*, Statista: The Statistics Portal (Jan. 9, 2018), https://www.statista.com/chart/12455/number-of-apps-available-in-leading-app-stores/. Many of these apps include the ability to purchase goods.

a hotel wireless network to watch a promotional video, order chocolate from a Parisian company delivered from Brussels to her cousin in North Dakota, and pay in pounds with her U.S. Bank of America credit card. As networks get more capacious and faster, as devices increase in power and ability, and with machine learning/artificial intelligence just beginning to provide useful assistance to Internet users, there is likely a myriad of future business models based on Internet connectivity that few can imagine today.

B. The Assertion Of State Jurisdiction On The Bases Of Virtual Technologies Will Eliminate Boundaries On State Sovereignty And Create 50 Subordinate Federal Governments

As noted above, there is no such identifiable physical "thing" called the Internet. It is a staggering concept to base state jurisdiction on Internet Protocol packets that travel through many different private networks between two users. This is particularly true when there is simply no precedent in history for such an overreach of state authority. The physical network of the U.S. Postal Service creates a far more concrete physical link between buyer and seller (as did the old switched network phone system) than the Internet. Precedent establishing the right of 50 states to regulate commerce with sellers in foreign and U.S. states doing business through a worldwide, distributed system (the Internet) will open a Pandora's Box of unimaginable consequences impacting both interstate and foreign commerce.

While most of the attention is focused on large catalog Internet sellers, the impact may be felt most directly on innovative start-up companies that cannot afford to interpret and apply the varying rules of some

50 states' regulatory regimes when creating new applications, crafting their business plans, and seeking capital.[18] The Internet has been an important engine of domestic and international economic growth. Saddling it with the regulatory burdens of 50 states may very well stall that growth and negatively impact our economy. The Internet economy's contribution to U.S. GDP is significant. In 2014, it doubled in seven years to nearly a trillion dollars creating three million jobs. *See New Report Calculates the Size of the Internet Economy*, The Internet Association (Dec. 10, 2015), https://internetasso ciation.org/121015econreport/; *see also* James Manyika & Charles Roxburgh, *The great transformer: The impact of the Internet on economic growth and prosperity* (Oct. 2011), https://www.mckin sey.com/industries/high-tech/our-insights/the-great-tr ansformer.[19] Creating a jurisdictional nexus between

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[18] This does not account for local taxing jurisdictions. Loudoun County, Virginia, for example, charges a one percent gross receipts tax on all entities doing business in the city. While 50 states' regulation of Internet business will be chilling enough for innovative startups, to launch a new Internet business becomes impossible if tens of thousands of local taxing entities are deemed to have jurisdiction for both taxation and administration of local use by such an expansion. For a more complete analysis of the daunting complexities and issues that locally administered use taxes impose in "home rule" states, see KPMG LLP, *Locally Administered Sales and Use Taxes*, Institute for Professionals in Taxation (2016), http://www.ipt.org/IPT/SponsoredResearch. aspx.

[19] The spread of Internet connectivity to other smart devices (the "Internet of Things" ("IoT")) is predicted to have an even greater positive impact on the U.S. economy. In 2015, two scholars wrote:

> The cost savings and productivity gains generated through "smart" device monitoring and adaptation are projected to create $1.1 trillion to $2.5 trillion in value

Internet entrepreneurs and 50 state governments will have a drastic negative impact on the growing Internet economy. Nor does the federal political system envision such a result. Those entrepreneurs and other e-commerce participants are not represented in the legislatures of all 50 states. The potential assertion of national jurisdiction through a rapidly expanding Internet, by the governments of all 50 states, is not a result contemplated by the federal system of government.

III. IN THE ABSENCE OF FEDERAL LEGISLATION GOVERNING TAXATION OF REMOTE SALES, THE REQUESTED ABROGATION OF *QUILL* THREATENS THE VIABILITY OF THE DIRECT MARKETING INDUSTRY

A. Remote Sales By Direct Marketers Is A Historical Business Model That Pre-Dates The Formation Of The Republic

The business practice of soliciting and effecting sales in interstate commerce by remote or out-of-state retailers[20] is a practice that pre-dates the Constitution

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> in the health care sector, $2.3 trillion to $11.6 trillion in global manufacturing, and $500 billion to $7.57 billion in municipal energy and service provision over the next decade. The total global impact of IoT technologies could generate anywhere from $2.7 trillion to $14.4 trillion in value by 2025.

A. Thierer & A. O'Sullivan, *Projecting the Growth and Economic Impact of the Internet of Things*, Mercatus Center: Technology Policy (June 15, 2015), https://www.mercatus.org/publication/projecting-growth-and-economic-impact-internet-things.

[20] The term "mail-order" refers to the "buying of goods or services by mail delivery." A mail-order business typically publishes a catalog containing a list of the merchandise sold by the

itself and even the formation of the Republic. Benjamin Franklin is believed to have been this country's first cataloger. *Mail-order business*, New World Encyclopedia, http://www.newworldencyclopedia.org/entry/Mail-order_business. In 1744, Mr. Franklin "formulated the basic mail-order concept" when he published a catalog of books for sale. *Id.*; Kelly Phillips Erb, *Flipping Through History: Online Retailers Owe Popularity and Tax Treatment to Mail Order Catalogs*, Forbes (Aug. 18, 2014, 10:10 PM), https://www.forbes.com/sites/kellyphillipserb/2014/08/18/flipping-through-history-online-retailers-owe-popularity-and-tax-treatment-to-mail-order-catalogs/#7b5b0f414ad9. His terms were cash only and books were available by mail. Erb, *supra*. He offered: "Those persons that live remote, by sending the Orders and Money to said B. Franklin may depend on the same justice as if present." *Id.*; Wendy Woloson, *How Benjamin Franklin Invented the Mail-Order Business*, Bloomberg (Mar. 13, 2013, 1:47 PM), https://www.bloomberg.com/view/ articles/2013-03-13/how-benjamin-franklin-invented-the-mail-order-business. Other early catalogs sold seeds to farmers. *Mail-order business*, New World Encyclopedia, *supra*. Some of the earliest mail-order enterprises or brands are still familiar names today: Hammacher Schlemmer (first catalog published 1848); the original Montgomery Ward[21] (first catalog published 1872); Sears, Roebuck & Co. (first catalog published 1894); Bloomingdale's (first catalog published 1885); and even Tiffany & Co. (*Blue book catalog* first published

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business. "Companies who publish and operate mail-order catalogs are referred to as catalogers in the industry." *Mail-order business*, New World Encyclopedia, *supra*.

[21] A subsidiary of Colony Brands acquired the "Montgomery Ward" brand (intellectual property) in 2008.

1845). *See* Erb, *supra*; *Mail-order business*, New World Encyclopedia, *supra*.

Mail-order businesses helped spur economic growth in America. Jim Gibbs, *Five Pivotal Moments in Catalog History*, The Dingley Press, http://dingley.com/five-pivotal-moments-in-catalog-history/ (last visited Apr. 1, 2018). Beginning in the late 1800s, mail-order businesses made it possible for retailers to get a wide variety of products from urban areas to rural America at competitive prices. Emilie Le Beau Lucchesi, *The Lost Charm of Mail-Order Catalogs in America*, CountryLiving (Oct. 25, 2016), https://www.countryliving.com/shopping/news/a40276/mail-order-catalogs/. Following both World Wars, consumerism rose and so did the use and distribution of catalogs. Divya Pahwa, *The History of the Catalog*, Medium (Aug. 15, 2014), https://medium.com/@pahwadivya/the-history-of-the-catalog-b5334841e941. The 1980s saw a boom in the retail catalog business. *Id.* Even today, with the advent of e-commerce, catalogs play an integral role in influencing American consumerism. *See id.*

B. The Imposition Of State Regulatory And Tax Obligations Occasioned By The Abrogation Of *Quill* Would Unduly Burden Catalog, Direct Mail, And Other Traditional Forms Of Solicitation, As Well As The Consumers That Purchase Through These Sale Methods

Ordering by mail did not disappear with the arrival of the Internet. For example, approximately 10 percent of Colony Brands' subsidaries' sales are still received via the mail, and some competitors have much higher percentages of orders received by mail. Some consumers send checks or cash (that certain marketers require to be sent with the order) along

with his or her order form, instead of including credit card information. There are many reasons why a consumer may choose to purchase via the mail, including lack of Internet access, privacy concerns, discomfort with the Internet, and other reasons. Abrogation of *Quill* would place undue and unnecessary burdens and expenses upon remote sellers with no presence in the state in connection with the forced collection of a use tax that is owed by a state's own residents simply because that state does not want to take the time or effort to collect it from its residents.[22]

This is so because the burden on a remote seller of calculating and being responsible for the proper collection of the myriad of sales and use taxes that may apply to a particular purchase made by a consumer in a particular state under the direct-mail business model is so great. Sales tax complexity has only increased since *Quill* was decided. Today, there are more than 12,000 taxing jurisdictions across the country, compared to the mere 6,000 that troubled the Court at the time of *Quill*. *Compare* Jaimy Ford, *Tracking Sales Tax Rates Across Thousands of Jurisdictions*, Avalara (June 25, 2015), https://www1.avalara.com/trustfile/en/blog/tracking-sales-tax-rates-across-thousands-of-jurisdictions.html, *with Quill*, 504 U.S. at 313 n.6. Collection of state and local taxes on

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[22] Several states have enacted notice and/or reporting laws that require remote sellers to notify their customers of obligations to pay use tax and/or to report summaries of the transactions annually to the customers and in some cases to the state department of revenue. The Tenth Circuit upheld this practice in *Direct Marketing Ass'n v. Brohl*, 814 F.3d 1129 (10th Cir. 2016) (holding that a state's notice and reporting requirements did not violate dormant Commerce Clause), *on remand from* 135 S. Ct. 1124 (2015). Adding further burdens on remote sellers by abrogating *Quill* is neither necessary nor justified.

the sale of goods sold via direct-mail catalogs or order advertisements is not merely burdensome. It is, in most cases, not *feasible* for the remote seller to be responsible for collecting and remitting the correct sales/use taxes. The proper tax to be paid on a single good depends on answers to a number of questions: What is the appropriate taxing district? Is the good taxable in that district? Are there any tax holidays? If taxable, what tax rate applies? Each of these questions evades easy resolution by a remote seller who must communicate with the out-of-state buyer about such taxes if the remote seller must collect and remit them, especially for orders mailed with payments. Identification of the appropriate taxing district is not clear-cut because taxing districts do not easily correlate to a county, city, or zip code. Determination of whether the good is taxable in that district is complicated by varying definitions of taxable goods categories and tax holidays. A decision as to what tax rate applies may depend on the type of product being purchased (*i.e.*, food versus household goods) and how the relevant taxing jurisdiction defines the good (which can vary from district to district). This analysis must be repeated for each product purchased via the mail.

The process is complicated enough for tax accountants with sophisticated software tools.[23] But for a consumer who wants to fill out his mail-order form and write a check, the process is impossible. Take the example of a consumer purchasing a single good via a catalog mail order. The consumer would have to find his taxing district from a list of 12,000 districts, which,

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[23] Proposed software solutions for online orders still ignore many other economic burdens and real-world complications that would be borne by out-of-state sellers.

if printed at a reasonable font size, would constitute a 40-page insert in the catalog itself. This insert would add considerable cost to the production and distribution of the catalog. The 40-page insert likely would not include information about the dates of back-to-school tax holidays or other special tax holidays, which could alter the amount of the tax owed. The 40-page insert would also not include rates for multiple tax categories, which means a catalog selling both food and household goods would need to include twice the information because many districts tax these items at different rates. The 40-page insert would not help the consumer determine to which category a good belongs because different taxing districts can define the exact same good in different ways. (A baseball hat may be clothing in one district, sports memorabilia in another, or a sun protection device in a third.)

Furthermore, if a consumer miscalculates the tax owed when sending payment with his or her order, the burden falls upon the cataloger to make it right. Overpayment of the tax obligates the cataloger to issue a refund,[24] complete with additional processing and postage costs not chargeable back to the consumer. Underpayment of the tax requires the cataloger to either cancel the order, delay fulfillment of the order until the additional tax payment is received, or take on the financial burden of paying the additional tax itself. There is no justification for placing these collection burdens on remote sellers who have no

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[24] The potential for overpayment of state and local taxes is not unique to the catalog industry or mail-in orders. *See Webster v. LLR, Inc.*, 2:17-cv-00225-DSC (W.D. Pa. filed Feb. 17, 2017) (class action lawsuit alleging consumer overpayments of sales taxes calculated based on location of consultant rather than location of consumer).

ability to influence the laws of states where they have no physical presence, instead of continuing to require the state's own residents to pay the proper use tax to their own state.

C. States Have No Authority To Impose On Internet Sales Regulatory And Tax Obligations Not Borne By More Traditional Means Of Direct Marketing

In its amicus brief in support of South Dakota, the United States suggests that one way to re-invent *Quill* in the age of e-commerce is to limit *Quill* "to its precise holding, involving traditional mail-order retailers whose only connection to a State is by mail or common carrier." U.S. Br. at 8. While *amicus* agrees that *Quill* should continue to apply to traditional mail-order retailers without a physical presence, having a website should not deprive any remote seller without a physical presence from the same protections absent Congress passing appropriate legislation setting precise rules.[25]

The United States' proposal to apply *Quill* only to traditional remote sellers (direct-mail marketers and catalogers), but not Internet vendors, has already been rejected by Congress. In 1998, Congress passed the Internet Tax Freedom Act ("ITFA") to prevent commerce over the Internet from being subjected to burdensome taxation. *See* Pub. L. No. 105–277, § 1100, 112 Stat. 2681-719 (1998) (made permanent in Pub. L. No. 114–125, § 922(a), 130 Stat. 281 (2016) (codified at

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[25] There are many details to be addressed in any future Congressional legislation in order to establish simple, clear, and fair rules for imposing such burdens on interstate commerce before requiring a remote seller without a physical presence to collect and remit sales taxes, including finding a solution for dealing with mailed-in orders with checks or cash as payments.

47 U.S.C. § 151 note)). Of particular importance here, ITFA *forbids* "[m]ultiple or discriminatory taxes on electronic commerce." ITFA, § 1101(a). Colony Brands agrees with other *amici* that the existence of ITFA, and its prohibition on discriminatory taxes on e-commerce, would, among other things, preclude this Court from adopting the United States' proposal. Certainly, a tax collection obligation that would apply to a chocolate bunny rabbit purchased over the Internet, but not the same chocolate bunny rabbit purchased out of a mail-order catalog is *per se* discriminatory and in violation of Federal law as embodied in ITFA. Absent new legislation by Congress, this Court should not retreat from *Quill*.

CONCLUSION

For these reasons, *amicus* Colony Brands respectfully urges this Court to affirm the decision of the South Dakota Supreme Court.

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